**Monetized Installment Sales – Executive Summary (Rev. 3/30/2020)**

## Overview

Sellers of real estate, businesses and other big-ticket assets face potentially large capital gains taxes. Depending on the state, the combined state and federal capital gains taxes can range from 20% to 33%. Sellers also may have to pay the Net Investment Income Tax, adding up to 3.8% to the total tax.

Sellers who want to defer their capital gains tax, for 30 years, and obtain cash at closing equivalent to 93.5% of their net sales proceeds, can achieve these results using a transaction structure known as a Monetized Installment Sale.

## How It Works

There are two steps to a Monetized Installment Sale that happen concurrently: a tax deferred installment sale, coupled with a tax-free loan.

## Installment Sale

The seller lines up a buyer for the asset, just as they normally would. Then, instead of selling directly to the end buyer, which would trigger capital gains tax, an intermediary buyer, known as a dealer, steps in between the seller and the end buyer, similar in concept to a 1031 exchange intermediary.

The dealer buys the asset from the seller using an installment sale agreement, with zero down, interest only payments for a term of 30 years, ending with a balloon payment of principal. This step defers the capital gains tax under Sec. 453 of the Internal Revenue Code, because the seller does not obtain constructive receipt of the sales proceeds until the dealer makes the final balloon payment of principal after 30 years.

The dealer immediately resells the asset to the originally intended end buyer, for cash. Title is transferred directly to the end buyer, with all representations and warranties remaining in effect. From the end buyer's perspective, it's as if the dealer was never involved in the transaction.

Upon close of this sale, the end buyer is now out of the picture. The cash from this sale is held in escrow until the seller completes the second part of the process, which is the monetization loan.

## Monetization Loan

While the cash from the sale to the end buyer sits in escrow, a 3rd party lender is brought to the table. The lender offers the seller a loan in an amount equal to 93.5% of their net sales proceeds (after closing costs). As with the installment sale, the term is 30 years, with interest only payments and a balloon payment of principal. The interest rate on the monetization loan is set so that its payments are equal to the payments the seller will be receiving from the dealer, so the payments end up being a wash.

The combined effect of the installment sale and the separate monetization loan is that, instead of paying the capital gains tax at time of sale, the seller now has the use of freely investable, non-taxable loan funds, in an amount that may be far greater than the after-tax proceeds from a taxable sale.

At the end of 30 years, the balloon payment on the monetization loan is funded by the balloon payment from the dealer. All that's left to do at the end of 30 years is to pay the capital gains tax, which can be funded using a portion of the monetization loan funds received by the seller, or whatever form of wealth they take after deploying those funds. This arrangement is illustrated in the diagram below.

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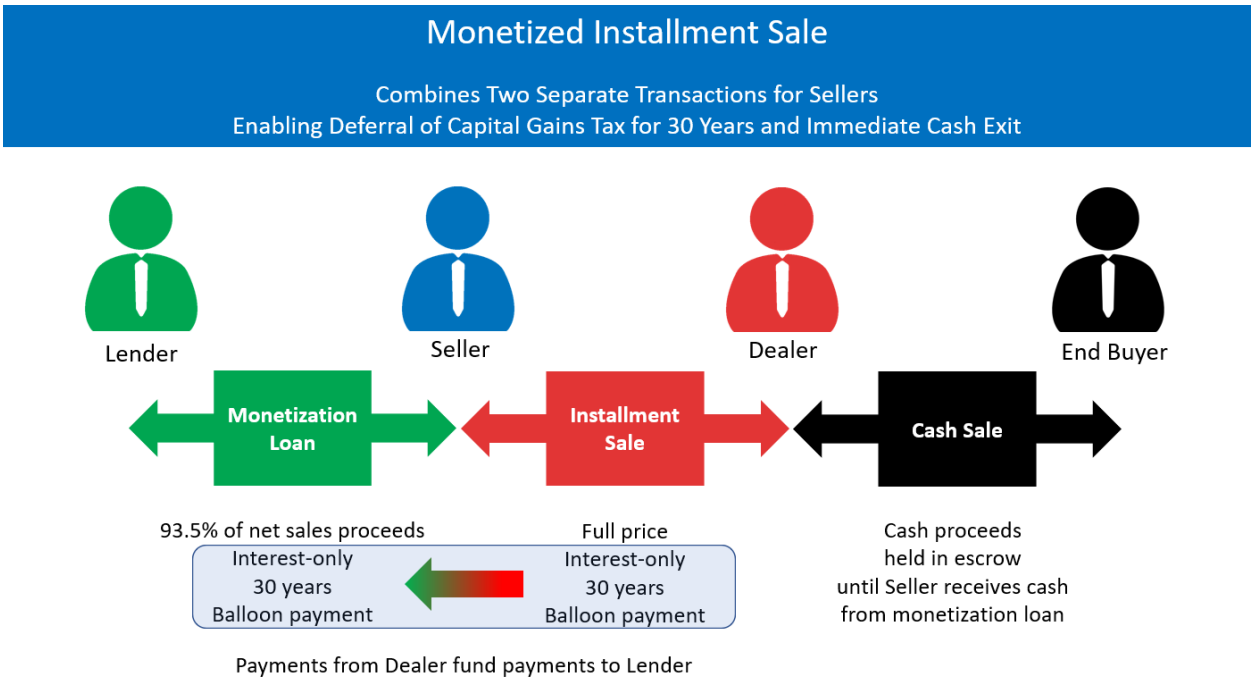


**Financial Benefit**

The seller gains the advantage of being able to freely invest, for 30 years, an amount equivalent to the capital gains tax that otherwise would have been due up front. The seller benefits from inflation and the time value of money. All the tax money not payed today can be invested for 30 years.

**Seller Protections**

The seller is protected if the dealer stops making payments to the seller on the installment contract, which provides that if the dealer doesn't pay the seller, the seller doesn't have to pay the lender. Additionally, the seller does not pledge any of their assets in this arrangement.

**History and Legal Basis**

Guidance from the IRS regarding monetized installment sales may be found in an IRS General Counsel Memorandum published in 2012, which reviewed and approved a monetized installment sale in a form that serves as the model for present-day monetized installment sales.

Monetized installment sales have been utilized by public companies for at least twenty years, with the approval of their boards, auditors and the SEC. A US Bankruptcy Court in California ordered use of a monetized installment sale in 2014 to help settle a case in which sale of real estate could produce cash.

**Uses**

Monetized installment sales may be used for tax-deferred sales of businesses, real estate, agricultural property, and virtually any highly appreciated asset other than publicly traded securities.

**For further information contact 415 Advisors at (866) 959-9969 or visit us at deferredcapitalgain.com.**